21 October 2011

Mr Felix Flinterman
Head of Unit: Credit Rating Agencies
European Securities and Markets Authority (ESMA)
103, rue de Grenelle, 75007
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FRANCE

<u>By Electronic Submission</u>

Dear Mr Flinterman

COMMENT ON ESMA'S DRAFT REGULATORY TECHNICAL STANDARDS ON THE PRESENTATION OF THE INFORMATION THAT CREDIT RATING AGENCIES SHALL DISCLOSE IN ACCORDANCE WITH ARTICLE 11(2) AND POINT 1 OF PART II OF SECTION E OF ANNEX I TO REGULATION (EC) NO 1060/2009 ("DRAFT RTS")

Moody's Investors Service ("MIS") has been an active participant in the testing phases of the new central repository for ratings data ("CEREP"). MIS would like to thank the CEREP team for their assistance provided to credit rating agencies ("CRAs") during this initial testing phase. A number of issues have arisen during this testing phase and it was our understanding that these issues would be resolved through the regulatory technical standards ("RTS"). However, we note that ESMA has not sought to address some of these issues through the Draft RTS and we would request that these matters be considered for inclusion in the resulting RTS but with an allowance of sufficient time for CRAs to implement any changes brought about to the existing reporting framework.

In this response, we note a number of general matters that we would propose be resolved in the resulting RTS. In Annex I, we have sought to raise a few technical points and also answered the questions posed in the Draft RTS.

1. Interpretation

    'CESR's Guidelines for the implementation of the central repository' (CESR Guidance") stated in paragraph C.2.2 that:

    > *In order to enable users of the CEREP to compare ratings of different structured finance asset classes of credit rating agencies, six asset classes including further subcategories have been defined. They are for reporting purposes of the CEREP only and do not interfere with the structured finance definition of the capital requirements directive (CRD).*

We note that there is no similar paragraph in the Draft RTS with the implication that ESMA will define a 'structured finance instrument' in the EU Regulation on Credit Rating Agencies ("the Regulation")[1] and consequently, 'securitisation' as the term is used in the Capital Requirements Directive ("CRD")[2] through Article 6 of the Draft RTS. Although MIS would not have an objection to a defined list of categories that ESMA would determine to be a 'structured finance instrument' because this would align the CEREP reporting requirements with the Regulation, we would suggest that such an interpretation be developed through guidance published by ESMA directly on this subject as opposed to indirectly through CEREP reporting requirements. A broader market consultation on the interpretation of the definition of a structured finance instrument may be required so as to ensure consistency of interpretation between the CRD and the Regulation.

Such an alignment will also solve the various technical issues arising through the implementation of the CEREP where, for example, a credit rating cannot be reported because it does not carry a structured finance indicator but falls within the reportable data fields for structured finance credit ratings in CEREP.

In the interim, we would propose that a similar qualification to that found in paragraph C.2.2 of the CESR Guidance is introduced into the resulting RTS.

2. Scope

MIS has advised ESMA that it is concerned that the total universe of credit ratings assigned by MIS may not be captured in data submitted to the CEREP. The most relevant sector that is excluded is that of covered bonds.[3] Although MIS would be able to report covered bonds under a programme or issuer basis for the purposes of CEREP reporting which would reduce the size of the universe of credit ratings that are not reported, MIS has been unable to do so because of the CEREP's inability to receive such data. We would request that the resulting RTS include a solution for these issues so that MIS is able to report its total rated universe to the CEREP and so ensure that the performance statistics generated by the CEREP accurately reflect the performance of our credit ratings.

3. Language

The CESR Guidance adopted an 'informal' tone which may be appropriate given the nature of the document. However, the adoption of an RTS requires a revision in favour of a more formal construction similar to that used in the drafting of EU regulations and directives. An example of language that could be rephrased would be Article 3 which prescribes that a CRA is responsible for the "accuracy, completeness and availability of reported data". There are multiple interpretations of this phrase. One interpretation suggests that a CRA must ensure the accuracy of the credit ratings it submits to CEREP whereas another interpretation suggests that a CRA must ensure that the data it submits matches the data housed on its internal systems. Furthermore, Article 7(3) requires

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[1] Regulation (EC) No 1060/2009 read with Regulation (EU) No 513/2011.
[2] Directives 2006/48/EC and 2006/49/EC.
[3] Other asset classes include certain structured notes, corporate ratings without an issuer rating and senior unsecured credit rating and U.S. municipal credit ratings without an issuer credit rating or tax-based credit rating.

CRAs to report an underlying debt credit rating where there is no issuer credit rating available for sovereign and public finance credit ratings. However, there is no guidance as to which debt rating should be disclosed if there are, for example, multiple long term debt ratings on secured and unsecured debt.

Concepts are introduced throughout the Draft RTS which are subject to interpretation and will make any implementation of the resulting RTS extremely challenging. This is of material concern to MIS because registered CRAs are subject to severe penalties for non-compliance with the Regulation. As an example, the Draft RTS distinguishes between Prime and Non-Prime RMBS in the reportable data. The concepts are not defined and there is no industry standard leading to the situation where an arranger may treat a structured finance instrument as a Prime RMBS deal, an investor as a Non-Prime and different CRAs classifying the categorisation differently depending on each CRA's methodology.

Therefore, holding CRAs to account for standards which are not objectively determinable sets a dangerous legislative precedent and may be subject to legal challenge at the time of an enforcement action which is a result which should not be the objective in establishing a regulatory framework.

4. Use of data

MIS notes that in the "Outline of the central repository and the main reporting features" that "ESMA does not disclose individual credit rating information to the public but statistics only". MIS supports the raw data approach adopted by the CEREP but on condition that such data is kept confidential by the CEREP under Article 32 of the Regulation. This construction is critical to ensure that the primary vehicle of disclosure of credit ratings is the publication vehicle of the relevant CRA and that the risk of multiple credit ratings (some of which may be outdated) are not released to the public which would cause material confusion in the market. Furthermore, MIS retains proprietary rights to the data which would be infringed if such data was to be made available by ESMA through the CEREP. MIS believes that it is critical that a provision protecting this right be included in the resulting RTS.

> *Data received by ESMA is protected under Article 32 of Regulation (EC) No 1060/2009 read with Regulation (EU) No 1095/2010 and may not be released to the public other than through aggregated performance statistics of the relevant CRA that would not identify underlying individual credit ratings.*

<p align="center">*****</p>

MIS would be pleased to discuss these issues and other technical and practical issues that have arisen from the implementation of the CEREP with the CEREP team before finalisation of the resulting RTS.

Yours sincerely

Frédéric Drevon
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A: Technical Comments

1. Article 3(2) requires that a CRA "shall be responsible for the accuracy, completeness and availability of the reported data". We understand "accuracy" to refer to the fact that the reported data to CEREP reflects the current outstanding credit rating at the time of reporting, or at such other time as may be specified. MIS would have a material concern if the term "accuracy" was meant to refer to the accuracy of the credit rating in terms of the credit opinion expressed. Furthermore, MIS is only able to submit data to CEREP where the system will allow for such reporting. Therefore, currently covered bonds are not able to be reported to the CEREP despite out willingness to submit the relevant raw data. Therefore we propose the following amendment:

   (2) A credit rating agency shall be responsible for ~~the accuracy, completeness and availability of its reported data~~:

   (a) submitting reports to the central repository that reflects the data on its ratings database for the relevant period under the report;
   (b) the completeness of data submitted to the central repository where such data may be reported within the central repository technical framework;
   (c) providing reports ~~It shall ensure that the reports are provided~~ in due time according to the file exchange principles specified in Article 12 using the reporting channels as described in Article 13 and following the reporting procedure stipulated in Article 14.

2. Article 4(4)

2.1 Article 4(4) should include the exemption provided in the response to Question 7 in the CEREP Newsletter Issue 2[4] that if a CRA does not have the information on certain mandatory fields for ratings issued prior to the year 2000 it should either complement the data or not report the data to the CEREP. MIS would urge ESMA to include this provision in the resulting RTS.

2.2 Article 4(4) provides an exemption for CRAs that have been in existence for at least the last ten years before the entry into force of Regulation (EC) No 1060/2009 if that CRA is able to demonstrate that the requirement is disproportionate given that CRA's scale and complexity. MIS would strongly propose that all registered CRAs be required to submit historical data in order to allow users to form an opinion on the performance of that CRA over time. The exemption provided by the draft RTS appears subjective and dangerously invites an opaque exemption consideration by ESMA. It is MIS's view that all registered CRAs that have been operating in the most recent ten years should equally be required to submit historical data to the CEREP. Failure to do this is likely to lead to data that is not comparable because those CRAs can simply exclude any effects of the most recent financial instability from performance statistics.

3. Article 5(4) states that "As long-term rating the issuer rating shall be reported". It is unclear how this provision should be interpreted.

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[4] December 2010.

4. Article 6(3) requires that a CRA shall report short-term ratings for ABCP. MIS publishes short-term ratings for structured finance in other asset classes, such as auto loans asset-backed securities. CRAs would find it helpful if the RTS could clarify as to whether only ABCP short-term ratings should be reported or all short-term ratings, including those assigned to other structured finance instruments.

5. Article 7(2) requires CRAs to report long-term debt credit ratings where an issuer credit rating is not available. MIS would find it helpful for the RTS to clarify which credit rating should be reported where there are multiple long-term debt credit ratings and no issuer credit rating.

    Furthermore, in terms of the CESR Guidance and following publication by the CEREP, CRAs were required to report long-term credit ratings for sovereign and public finance ratings. It would appear from the Draft RTS that CRAs will be required to report short-term credit ratings for sovereign and public finance ratings. MIS uses three rating categories for short-term municipal obligations that are considered investment grade. These ratings are designated as Municipal Investment Grade (MIG) and are divided into three levels — MIG 1 through MIG 3. If these credit ratings are required to be reported to CEREP, MIS would require additional time to implement this change to its systems, including the submission of a new rating scale to CEREP. We would request that if such a change is introduced through the resulting RTS, that CRAs be provided with adequate time of at least six months in which to prepare for the submission of this new category of data.

6. Article 8(1) limits the rating scales that may be used for reporting purposes into the CEREP. MIS is concerned that rating scales adopted by a CRA should not be limited in any way and especially not through the resulting RTS. Such a provision would be at risk of being *ultra vires* article 21 of the Regulation. We would propose that the CEREP be constructed with sufficient capacity to allow for a reasonable number of rating scales to be reported into the CEREP but not that the resulting RTS restricts the number of rating scales adopted by a CRA.

7. Article 9(2)(b)

    According to CESR Guidance[5] a rating flagged as default during a reporting period and withdrawn for reason 2 after one or several periods should be flagged again as a default. This solution was recognised as creating an issue because effectively a default would be double-counted. ESMA informed MIS that this issue would be corrected in the next release of CEREP. MIS would propose that ESMA consider resolving this issue through the resulting RTS.

8. Annex 1, Table1, Field 4

    It should be noted that MIS adopts different unsolicited policies outside of the EU which affects the status of non-EU endorsed credit ratings as unsolicited/solicited.

9. Annex 1, Table 1, Field 12

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[5] See the definition of default, page 40.

A rating scale may typically apply to all types of ratings. It is unclear how this should be reported and we propose an additional standard: "A" in case the rating scale is applicable to all types of credit ratings.

10. Annex 2, Table 1, fields 3, 4, 5 and 6, column "Type".

The list of structured finance asset classes in Article 6 includes asset classes where only an issuer credit rating may be assigned. For example, in addition to the credit rating on a structured investment vehicle, a credit rating on a derivative product company is also at issuer level. We propose that the fields be amended as follows:

Mandatory. Applicable only for <u>ratings reported at issue level</u> ~~structured finance (not SIV) ratings~~.

Optional. Applicable only for ~~structured finance (not SIV)~~ ratings <u>reported at issue level</u>.

Mandatory. Applicable only for ~~corporate, sovereign and public finance, and structured finance issuer SIV~~ <u>ratings reported at issuer level</u>.

Optional. Applicable only for ~~corporate, public finance and SIV~~ <u>ratings reported at issuer level</u>.

11. Annex 2, Table 1 Field 14

It would be helpful if the definition of the location of the rating as adopted in "CESR's Guidance on the Registration Process and related issues" was re-iterated in the resulting RTS.

12. Annex 2, Table 1, Field 17

Additional clarification on the methodology for determining the country code of the rated instrument would be necessary in the resulting RTS.

MIS would also propose that the RTS should note that the ISO code "ZZ" should be used when the country code is "International" (as previously provided through CEREP Newsletter No. 3).[6]

13. Annex 2, Table 1, Field 21

The terms adopted by the CEREP in distinguishing between, for example, prime and non-prime RMBS are not defined through an industry standard and we would request ESMA to reconsider how to create the necessary certainty through the use of terminology in the resulting RTS.

We assume that the acronym for "non-prime RMBS" should be "NPR" as opposed to "NRR" as currently drafted.

14. Annex 2, Table 1, Field 22

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[6] See Question 17.

We would propose additional guidance as to how this field should be reported in, for example, the case of an ABCP transaction where short-term notes are issued on a rolling basis but receive the same credit rating. A new credit rating is not physically assigned for each new ISIN. The report into ESMA will therefore show issuance of YYYY but following a rating action, the vintage would actually be YYYY+2, for example. This would extend to the ratings on tap issuance and restructurings.

15. Annex 2, Table 1, Field 25

It is not clear what reasons may be offered by CRAs when reporting a credit rating for a previously reported period.

16. Annex 2, Table 2, Field 2

It is not clear what reasons may be offered by CRAs when reporting a reason for historic cancellation.

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B: Questions

Q1: Do you think that the chosen structure of the Regulatory Technical Standards is appropriate? In particular, what is your view on the balance of provisions set out in the text of the Regulatory Technical Standard and the annexes?

As noted above, MIS is concerned that the language structure and lack of defined terms will create loose subjective standards against which CRAs will be held accountable under enforcement actions. MIS would request ESMA to consider publishing the framework for the CEREP excluding the Annexes and for the Annexes to take the form of ESMA Guidance.

Q2: Do you think that the level of detail of the Regulatory Technical Standards is appropriate?

MIS believes that the CEREP is sufficiently detailed in order to achieve its objectives as set out in paragraph 8 in the Outline of the central repository and the main reporting features, however, we believe that the explanatory detail on the requirements could be significantly enhanced through a taxonomy in order to ensure that CRAs have sufficient clarity on the CEREP reporting requirements to meet their regulatory obligations.

Q3: Do you think that ESMA did cover all relevant items?

MIS is concerned that although all the relevant items are captured, the scope of data that CRAs is able to submit to the CEREP is limited because of system constraints at CEREP. MIS is hopeful that these system issues are resolved before the resulting RTS enters into force.

Q4: Is it possible that a credit rating agency does not know the 'Responsible CRA unique identifier'? See field 23 in Table 1 of Annex 2 to the Regulatory Technical Standards.

There is a risk that a CRA may not have a BIC Code.